Available online at www.sciencedirect.com
SCIENCE DIRECT®
ELSEVIER
Journal of Asian Economics 16 (2005) 807–816
JOURNAL OF ASIAN ECONOMICS

Celebration of Kazuo Sato's Life

Household and financial institution planning in Japan: Corporate governance by citizens

Masumi Kishi

Faculty of Commerce, Chuo University, Higashinakano, 742-1 Hachioji, Tokyo 192-0393, Japan

Abstract

At present, the Japanese economy is transforming from an industrial to a civil society. This paper discusses the financial system of corporate governance based on citizens' participation, which enhances the welfare of households, referring to late Professor Kazuo Sato's numerous contributions to the Japanese economy and monetary policy. In order to raise the interests of households, we found it necessary to specifically target the management efficiency of Japanese financial institutions and the method by which profit rates rise due to the unique participation of citizens and households, in other words, the inhabitants of the community. This is seen in the case of bonds as they are related to the environment, filling the needs of the inhabitants of the community; we will focus on the role of the bond market to complement indirect finance.

Keywords: Household and financial institution; Corporate governance; Citizens

1. Introduction

It is an indispensable fact that institutions – financial and nonfinancial – must raise their profits and pay higher dividends to investors in order to realize their financial goals. But these profits still languish at low levels in the current investment climate, which has seen depreciation due to bad loans. Because of weak profit margins, the government has come to the rescue, liberating financial policies and promoting globalization, yet at the same time, without imposing regulation: disclosure and rating systems, for example. As a result, various financial reforms, begun since the late 1990s, aim toward efficient management by tightening regulatory policies.

But this is not so easily accomplished over time. Strengthening corporate governance, characterized by citizens' participation, as well as rationalization of management, may be the way out of this situation; namely, this involves the participation of the citizen as an investor and a depositor, in other words, the participation of the inhabitants of the community. This might shape

E-mail address: vinomac@tamacc.chuo-u.ac.jp.

1049-0078/$ – see front matter © 2005 Published by Elsevier Inc.
doi:10.1016/j.asieco.2005.08.002

a more economically functional society, increasing the interests of both financial institutions, enterprises and households.

Therefore, this paper seeks to consider how to improve the investment environment for individual households in light of corporate governance, based on citizens' participation within the changing structure of the society, from an ''industrial'' to a ''civil'' one. This seems urgent.

In Section 2, we shall survey the characteristics and problems encountered by Japanese households confronted with an aging society, comparing then to the portfolios of U.S. households. In Section 3, we shall consider management strategies of financial institutions, while taking into account governmental policies aimed at strengthening prudential regulations. Accordingly, in Section 4, we will argue that the best policy is to have corporate governance, assuming the participation of citizens as investors or depositors. And in the final section, we shall summarize our discussion.

2. Life planning and financial assets

Let us examine the portfolios of Japanese households. According to the survey by the Central Council for Financial Services Information, the average household savings in Japan was about ¥14 million (US$ 134,423 at the change rate of ¥104 to US$ 1) in 2004.[1] Of the total savings, the share of deposits at banks was 41.5%, which was the highest share of all financial assets held by households, while the share of postal savings together was a 18.6%. Therefore, the share of bank deposits and postal savings was total of 60.1%.

The rationale of most households was to save for: (1) old age, education and housing; (2) a cushion for sickness or disaster; and (3) Investment. Households invest their funds according to the following equation, in order to realize the above purposes:

$$\text{net worth} = \text{real assets} + \text{financial assets} - \text{financial liabilities} \tag{1}$$

Households hold their assets as the form of real assets, such as housing and buildings on the one hand, and monetary assets (currency, bank deposits, and postal savings) and nonmonetary assets (e.g., bonds, stocks, and life insurance) on the other, while they hold liabilities such as home loans and consumer loans. Although, households select their portfolio based on their life plans, the actual Japanese household balance sheets from 1970 to 2002 are shown in Table 1. According to this table, we can observe the following: (1) real assets (land and other tangible assets) were sharply reduced after the collapse of the bubble of 1990; (2) long-term bonds, stock, and insurance increased remarkably.

Let us consider the reason why portfolio selection of households changed, according to Sato's wealth target hypothesis (Sato, 1989, 1995). Required savings, which is the difference between target amount of savings and real amount of savings, are shown as follows:

$$s = \lambda[a^{*}a_{-1}] \tag{2}$$

where S denotes present amount of savings; Y, income; A^{*}, target amount of savings; and A_{-1} denotes real amount of savings at initial time.

$$\text{Also}, s = \frac{S}{Y}, a^{*} = \frac{A^{*}}{Y}, a_{-1} = \frac{A_{-1}}{Y}, \lambda = \frac{1}{T}$$

where T denotes the planning horizon.

[1] As to this data, see http://www.Saveinfo.or.gp/.